COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS & ENERGY

Petition of Boston Gas Company d/b/a KeySpan Energy Delivery New England, pursuant to General Laws Chapter 164, § 94, and 220 C.M.R. §§ 5.00 et seq. for a general increase in gas rates.	D.T.E. 03-40

INITIAL BRIEF OF THE MASSACHUSETTS OILHEAT COUNCIL, INC. AND THE MASSACHUSETTS ALLIANCE FOR FAIR COMPETITION, INC.

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Table of Contents

Table of Contents (continued)

Table of Cases and Authorities

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I. INTRODUCTION

This initial brief is filed on behalf of the Massachusetts Oilheat Council, Inc. (MOC) and the Massachusetts Alliance for Fair Competition, Inc. (Alliance) in accordance with the procedural schedule established by the Department of Telecommunications and Energy (Department) in this proceeding. MOC and the Alliance (collectively referred to as "intervenors") submit this initial brief responding to the petition of the Boston Gas Company d/b/a KeySpan Energy Delivery New England ("Boston Gas", "Company" or "Utility") seeking approval of both a $61.3 million rate increase and a performance base rate plan. The intervenors intend to address ratemaking and policy issues concerning the Company's promotional advertising and incentives, free equipment promotion, trade ally programs, affiliate conduct, and requirements for interruptible customers.

II. IDENTITY OF THE INTERVENORS

MOC is a not-for-profit trade association representing independent marketers, distributors and retailers of heating oil, other petroleum-based products, heating equipment and related products and services. Its members supply and service residential, commercial and industrial consumers throughout the Commonwealth of Massachusetts. MOC's members provide these products and services to customers within the service territory of, and in competition with, the utility and its affiliates.

The Alliance is a coalition of small plumbing, electrical contracting, heating, ventilation and air conditioning (HVAC) businesses. Its members provide installation, repair and maintenance services of HVAC equipment and related products and services to residential and commercial customers in the Commonwealth. Alliance members provide these products and services to customers within the service territory of, and in competition with, the Company and its affiliates.

III. PROCEDURAL HISTORY AND OVERVIEW OF THE PETITION

On or about April 16, 2003, the Company filed tariffs and a petition with the Department seeking (1) to increase its base rates by approximately $61.3 million, an approximate 9.59% increase in the Company's annual total revenues to become effective May 1, 2003. (Exhibit KEDNE/JFB-1 p.3); and (2) approval for a price cap performance-rate plan under which the Company proposes to adjust its rates annually for five years. (Id.) The Department docketed this matter as D.T.E. 03-40, suspended the effective date of the requested rate increase until November 1, 2003 and commenced an investigation into the propriety of the Company's filing.

On May 15, 2003, MOC and the Alliance petitioned for leave to participate as parties in this proceeding. From May 19, 2003 to May 22, 2003, the Department conducted public hearings on the Company's proposal. On May 23, 2003, the Department convened a procedural conference to establish a schedule for discovery, hearings and brief. At this conference, the Department granted the petition of MOC and the Alliance to intervene as full party participants.

The Department conducted evidentiary hearings commencing on June 26, 2003, until August 11, 2003. This Initial Brief is filed consistent with the Department's procedural schedule and its order dated August 21, 2003.

IV. **PRELIMINARY STATEMENT**

Prior to addressing individual issues, several comments must be made concerning the particular rate filing and the Company's operations.

A significant aspect of this rate filing is the Company's proposed annual promotional expense of just over $13 million. This represents a $9.4 million increase over the Company's prior approval promotional expense, and constitutes approximately 15% of the total increase demanded in this case. Over five years, the proposed total promotional expense added to the cost of services would be $65,131,540 (TR 2242). The enormity of the Company's proposed promotional expense demands a stricter evaluation. Thus, in reviewing the Company's unprecedented request, the intervenors respectfully request that the Department consider the following factors.

Initially, in evaluating the promotional programs of the Company which are designed exclusively to add customers and attach load to the Company's system, the intervenors respectfully request that the Department consider and evaluate the current status of the natural gas industry and deny rate recovery for such programs. As discussed more fully below, the intervenors believe that the Company's aggressive promotional conversion campaign is ill-advised amid the current concerns of supplies and price of natural gas. This is especially so with respect to the impacts of such promotions upon new customers.

Next, MOC and the Alliance believe that as part of its rate review, the Department should take into consideration the impact of the Company's rate-based promotional programs upon the unregulated competitive markets. The intervenors are not requesting antitrust or unfair trade relief. Instead, the intervenors believe that the overall public interest of the Commonwealth would be served by the Department's recognition that the Company's monopoly status as an LDC enables it, unlike any competitor in non-regulated marketplaces, to influence and leverage the marketplace to achieve goals that no other competitor can. As energy markets become more interdependent and also move toward competition, a monopoly's ratepayer funded activities that occur in unregulated markets should be scrutinized for its affect upon the market.

Finally, we respectfully request that the Department consider whether the promotional expenses sought to be approved are properly recoverable through rates. Utilities in the past have justified such expenses on the belief that any addition to the customer base automatically benefits all ratepayers. As the Department is aware, this oft cited principle is not always true. (See for example Berkshire Gas D.T.E. 01-56 [2002]). MOC and the Alliance urge that any promotional program or incentive that does not provide both a true direct benefit and a net economic benefit to the ratepayer be excluded from the cost of service.

V. RELIEF REQUESTED

Through this brief, intervenors respectfully request the following relief:

- that given the current state of the natural gas industry, the Company should inform potential conversion customers responding to free incentive offers to consider the possibility of high gas prices in making their decision;
- that all expenses associated with the Company's free equipment program be excluded from the cost of service;
- that all expenses associated with the Company's VPI program be excluded from the cost of service;
- that all expenses associated with rebates and other incentives be excluded from the cost of service;
- that all advertising costs that do not meet statutory and Department requirements be excluded from the cost of service;
- that the Department order the Company to provide all potential conversion customers with a statement disclosing full conversion costs, a payback analysis, and full disclosure of the Company's guarantee;
- that the Department order that any of the Company's unregulated HVAC affiliates must have names that are different from the KeySpan Company name; and

- that new and existing interruptible customers have adequate backup supplies of alternate fuel available for periods of interruption.

VI. ARGUMENT

A. THE STANDARD OF REVIEW

Pursuant to G.L. c 164, §94, the Department must review rate increase proposals by a utility company to determine whether the proposed rates are just and reasonable. Berkshire Gas Co. D.P.U. 96-67 (1996), p. 6. The burden of proving that a proposed increase is justified falls upon the utility. Town of Hingham v. Department of Telecommunications and Energy, 433 Mass. 198 (2001). A utility's filing of a rate case places the Company on notice that every element of its filing is at issue, and the burden is upon the Company to demonstrate that the expenditures made are reasonable and just. Bay State Gas Company, D.P.U. 1535 (1983), pp. 14-17. If the Company fails to meet this burden, the Department must deny the requested rate treatment for any proposed adjustment. Fitchberg Gas & Electric Light Company v. Department of Public Utilities, 375 Mass. 571, 582-583 (1978).

B. COST OF SERVICE - THE COMPANY'S PROMOTIONAL EXPENSE REQUEST SHOULD BE REJECTED

The Company is seeking approval from the D.T.E. to recover an annual amount of $13,026,308 through rates for its sales promotion expenses. (Ex. MOC 1-2; TR 2242).

Most of the promotional expenses comprising the $13 million figure are related to the Company's free equipment program used to entice residential and commercial customers to convert to natural gas. Other components of the proposed promotional expense include advertising, rebates (i.e., customer rebates for larger boiler conversions and special equipment, oil tank removal rebates and others), costs associated with the Company's Value Plus Installer Program (VPI) and other incentives (Ex. AG 23-1). Presently, the company recovers promotional expenses totaling $3,632,931 through rates set in its prior case Boston Gas D.P.U. 96-50 (Ex. MOC 1-1). The Company has not met its burden and proven why a $9.4 million annual increase in promotional expenses is necessary.

1. The Department Should Consider The Current State Of The Natural Gas Industry, Deny Rate Recovery Of The Company's Promotional Expenses, And Inform Consumers Of Price Concerns

Before permitting the Company to recover from ratepayers the Company's promotional expenses, including the costs of the free equipment and VPI programs, the Department should evaluate and review the existing concerns over the supply and price of natural gas.

Over the recent months there has been tremendous media coverage reporting industry and government concerns with the supply and price of natural gas for the near future. The growth of natural gas consumption over the past years has been dramatic, particularly for large volume users and electric generators. In the northeast, the winter of 2002-2003 created a severe strain on all heating energy resources. As a result of the demand for gas during the winter, and for other reasons, natural gas supplies became tight and prices began to increase. In response, Congress convened hearings to investigate the problem and identify possible solutions. Treasury Chairman Alan Greenspan summarized the concerns at a Congressional hearing in June:

> In recent months, in response to very tight supplies, prices of natural gas have increased sharply. Working gas in storage is currently at very low levels relative to its seasonal norm because of a colder-than-average winter and a seemingly inability of increased gas well drilling to significantly augment net marketed production…
>
> Today's tight natural gas markets have been a long time in coming, and futures prices suggest that we are not apt to return to earlier periods of relative abundance and low prices any time soon.

Ex. MOC 4-1 - Attachment - <u>Testimony of the Honorable Alan Greenspan before the House Committee on Energy and Commerce</u> (June 10, 2003), p. 1.

Testifying before the same House Committee on Energy and Commerce on June 10, 2003, the American Gas Association (AGA) representative stated:

> Since the beginning of this year, natural gas has been trading in wellhead markets throughout the nation at prices floating between $5 and $6 per thousand cubic feet. This has not been a "price spike" of the sort we have seen in the past lasting several days or perhaps several weeks. Rather it has been sustained over a period of several months. And there is no sign that it will abate in the near future. Indeed, quotes for future's prices on NYMEX over the next 24 months have reached a consistent record level mirroring current cash prices.

Ex. MOC 4-2 - Attachment - <u>Testimony of Mr. Carl L. English, President and Chief Executive Officer of Consumers Energy on behalf of AGA before the House Committee on Energy and Commerce</u> (June 10, 2003), p. 2.

The AGA representative noted that the industry needs gas prices to fall between

$2.50 and $3.00 per thousand cubic feet in order to remain competitive. He further explained that industrial and business customers very quickly feel increases in prices while residential customers who rely upon their local utilities will not begin to feel current high gas prices for months (Id.):

> From the point of view of the residential consumer, some families will pay hundreds of dollars more to heat their homes this winter, which will be hundreds less to spend on other things. Families will again be forced to make difficult decisions between paying the gas bill, buying a car, or saving for future college educations. There are, of course, state and federal programs such as LIHEAP to assist the most needy. This winter the potential price increases will affect all families - those on fixed income, the working core, and the lower-income group, we well as those caught between living comfortably and living day to day.

(Id. p. 2).

No one can fully predict energy prices, even short term. However, the AGA representative was worried that prices this Fall and Winter could "unleash a firestorm of protests" as some consumers see their natural gas bills double. (Id.). Moreover, at a Senate hearing in July, 2003, the Federal Chairman reiterated his belief that gas prices would not be dropping anytime soon. To address this crisis, House Speaker Dennis Hastert announced the formation of the "Task Force for Affordable Natural Gas" on July 10, 2003.

Recent figures released by the U.S. Department of Energy's Energy Information Administration (EIA) indicate that NYMEX natural gas futures settled at $5.179 per MMBtu for September delivery and $5.234 per MMBtu for October delivery as of August 13, 2003. EIA, Natural Gas Weekly Update - Thursday, August 14, 2003. EIA reported that "the price for delivery off Tennessee Gas Pipeline in New England gained 44 cents per MMBtu to

$5.69". (Id.) EIA predicts that wellhead prices of gas will range between $4.24 and $4.74 per MMBtu through the end of 2003. (Id.). As of August 20, 2003, NYMEX natural gas futures for September delivery had dropped slightly to $5.119 per MMBtu. EIA Natural Gas Weekly Update - Thursday, August 21, 2003. EIA also reported that:

> Futures prices for delivery in months through March 2004 all settled above $5, with the highest price gas for future delivery over this period as of yesterday being for January 2004, at $5.726 per MMBtu.

Id. There is little doubt that high gas prices will be experienced this coming winter season.

Directly related to price concerns is the supply situation of natural gas. The low inventory levels witnessed at the beginning of the summer caused great concern for supply. Storage refill levels in the Northeast have proceeded at an expeditious pace since June and inventory levels are slightly low proceeding into the heating season. EIA reported that the inventory levels which in June were 25% less than the five year average inventory level, are now 7.4% less than the five year average for the week of August 20, 2003 (Id.). For the East region, the deficiency in inventory levels is 7.3% (Id.). While storage levels are increasing, inventory levels alone do not mean that a supply issue does not exist:

> For the past three years, natural gas production has had to operate full-tilt to meet consumer demand. The "surplus deliverability" or "gas bubble" of the late 1980's and 1990's is simply gone. No longer is demand met while unneeded production facilities sit idle. No longer can new demand be met by simply opening the valve a few turns. The valves have been, and are today, wide open.

(Ex. MOC 4-2 - Attachment.)

A severe winter, increased demand by firm customers, or greater need by electric generators are examples of events that could strain the supply of gas and drive prices higher. Although the exact nature and extent of the impact of the supply and price difficulties faced by the natural gas industry in general and by the Company in particular are not fully known, we know that the immediate future is grim. What is also known is that the Company intends to continue its aggressive promotion of conversions and adding load from alternate fuel sources to natural gas despite the concerns and warnings. In the test year alone, the Company added 2,118,017 mcf of gas from 12,554 conversion customers of which 1,178,774 mcf was related to residential customers (Ex. MOC 1-3 - Attachment 2002 NGA survey of New England Natural Gas Customers). For 2003, the Company projects that it will add another 12,963 customers of which 10,844 will be residential and 2,119 commercial. (Ex. MOC 2-8). The Company estimates that the projected volume to meet the needs of these new customers will be 76,113,350 mcf over the anticipated life of the additions (RR-MOC-3).

The Company not only intends to continue its conversion promotions unabated, it freely admits that it has not conducted any analysis or evaluation to determine the level of natural gas price and/or constrained supply at which the Company would alter or cease its promotional activities. (Ex. MOC 4-3 and 4-4; TR 2262-2263). The Company does not believe that there are any supply concerns. (Id.).

The Company's position is surprising given the current level of apprehension for the industry. Regardless of how well the Company has planned, the price of natural gas will be directly impacted and influenced by local, regional and national use. The Company also cannot predict whether one or more factors (i.e. a severe winter) would constrain resupply of its volumes needed to meet peak demand.

Proposed solutions to the natural gas crisis all seem to focus on the supply side. Recommendations involve mostly advocating for increased exploration and production of natural gas. There has been little discussion of the demand side of the issue, even though Chairman Greenspan stated "to the extent that natural gas consumption must adjust to limited supplies, most of the reduction must come from the industrial sector and, to a lesser extent, utilities." (Attachment to Ex. MOC 4-1, p. 1). The elimination or reduction of dramatic demand increases associated with adding load would mitigate the current situation. While intervenors do not suggest that customers of the Commonwealth be denied their freedom of choice for fuel, the Company should not be permitted rate recovery for its aggressive conversion programs in this climate. Where adding load and demand to the Company's system could detrimentally affect ratepayers in terms of price and/or supply, it would be imprudent for ratepayers to bear the cost of the Company's exorbitant promotional expenses.

In addition to the impacts upon the ratepayer, rate recovery is inappropriate from the perspective of the new customer. The Department's traditional analysis of promotional programs concentrates on ratepayer benefits and not whether the conversion is personally beneficial for the individual customer. While this should be an important consideration at any time, this is extremely significant at present because of the predicted high price of natural gas in the near future. Customers convinced to convert to natural gas because of the Company's promotional incentives could be shocked at the price of gas upon receipt of their first winter bill. The Department should disallow rate recovery for promotional programs that encourages customers to convert to a fuel that is forecast to be extremely high compared with historic levels.

Additionally, the forecasted price levels for natural gas require that potential conversion customers who are lured by free equipment and rebate offers ("free incentives") be provided with information regarding potential price impacts for the near future. At present, the Company only provides price information when asked (Ex MOC 2-2). The only written material the Company presents to the potential conversion customer are two documents that compare the price of oil versus natural gas (Id.) These documents are out of date, do not reflect the current price of natural gas, and presently would have the effect of misleading customers into believing that gas prices will be comparable to past average prices. Without complete information, potential customers responding to the promises of free equipment, rebate offers, and other incentives are most at risk of undertaking an uneconomic conversion.

In order to provide customers will full disclosure, MOC and the Alliance request that the Company be required to inform potential customers who respond to free incentive offers that the possibility of high gas prices should be considered when deciding to undertake a conversion. This could be accomplished through a statement included on free incentive promotional materials or in addition to the disclosure and payback materials given to individual customers as proposed below.(See Part VI.C.). Such disclosure will provide customers with vital information prior to converting. Moreover, the price information is necessary because the Company intends to continue promoting free incentives to attract customers regardless of price and supply considerations.

The wisdom of adding load in this present climate is suspect at best. The Department should not sanction such activities by permitting the promotional expenses to be recovered through rates. Consequently, we urge the Department to evaluate the current price/supply concerns of the industry as it relates to the Company, examine the rate treatment of all promotional programs in light of these price/supply concerns, deny rate recovery for promotional incentives, and order that price information be provided to customers responding to free incentive offers.

2. All Costs And Expenses Associated With The Company's Free Equipment Program Should Be Disallowed From Rates

The most significant incentive program already in existence and proposed to be recovered through rates is the Company's free equipment program. In the test year, the Company spent $6,183,540 on the equipment for the program. (Ex. MOC 1-1).[1] This is only the cost of the equipment and does not include labor, fringe benefits and other costs also being sought by the Company. The exact number has not been specified but is a substantial portion of the $11,547,007 the Company provided for its non-advertising marketing expenses. (See Ex. AG 23-1).[2]

To our knowledge, the Department has never evaluated a promotional program as immense in scope and magnitude as this Company's free equipment program. As previously noted, we believe that the Department, in fulfillment of its public interest

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[1] This number appears to be the total amount for the entire KeySpan NE territory (Boston Gas, Colonial and Essex) (See RR MOC #1). The Company may have misstated that the entire amount was attributed to Boston Gas customers. (Ex. MOC 1-14).

[2] This breakout of Account 912 also include expenses associated with the utility's VPI program, trade shows, and rebates.

obligation, should take into account the effects of such programs on the competitive marketplace, on new customers, and in light of the current state of the natural gas industry. Nonetheless, for purposes of this point – and the next – we will focus on the Company's proposed free equipment program as it relates to the ratepayer.

There exists no specific statutory guidance for the ratemaking treatment of non-advertising promotional programs. Consistent with the public interest, and to assure that only reasonable expenses are recovered through rates, the Department has articulated that promotional expenses must directly benefit ratepayers to be recoverable. Boston Gas D.P.U. 93-60, p. 159. The Department has also stated that incentive programs must provide net benefits to ratepayers to qualify for cost recovery. Berkshire Gas D.T.E. 01-56 (2002). Consequently, the Company's incentive programs should satisfy a two-step test to qualify for rate recovery. The Company must meet a threshold burden that the particular program provides a true direct benefit to the ratepayer. Should the Company satisfy this initial burden, then it must demonstrate through a clear cost/benefit analysis that there is an economic net benefit to the ratepayer in order to include the incentive expenses in rates. Berkshire Gas D.T.E. 01-56 (2002). With regard to the free equipment program, the Company has satisfied neither burden.

The ratepayers do not directly benefit from the Company's free equipment program. The term "direct" means that there is nothing intervening between the offerings of the free program (free equipment) and the benefit enjoyed by the ratepayer. It implies that the program should provide an immediate advantage and value to the ratepayer and that the ratepayer will experience first-hand, personal gains.

The Company's justification for including the free equipment program is the alleged advantage of securing additional customers. This is, at most, an indirect benefit to ratepayers. The free equipment program is devoted exclusively to prospective customers. Current customers of the utility wishing to replace or upgrade their heating equipment cannot take advantage of the program as it is not even offered to existing customers. (TR 2254). Ratepayers receive no personal benefit from the program. They are promised the alleged indirect benefit of the added load to the system that may in the future, if market conditions are right, provide an increased rate base. This cannot be considered a direct benefit.

In addition, the intervenors dispute that the free equipment program provides any economic net benefits to the ratepayers. The Company has not satisfied the net benefits test to justify rate recovery for the free equipment program. Instead of performing a cost/benefit analysis as discussed in Berkshire Gas (D.T.E. 01-56 and D.T.E. 01-56A [2002]), the Company has set forth its own calculations.

The Company claims that it has met the net benefits test by taking all capital investments, including promotional costs, and calculated an 18.8% internal rate of return (IRR) (Ex. KEDNE/PJM-9; TR 3438-3439). Since, claims the Company, the IRR is greater than the allowed rate of return, ratepayers benefit by "lowering costs to all customers" (TR 3438-3439). In calculating its IRR, the Company used a useful life of 25 years for residential and 15 years for commercial load (Ex. DTE 4-28). The Company's analysis is insufficient to prove that ratepayers enjoy a net benefit from the free equipment program.

The Company's approach suffers from the deficiency that all capital investments are aggregated. For projects over $100,000, the Company submitted a table of "Revenue

Producing Investments" that lists the IRR associated with each project for both total capital investment and marginal capital investment. (Ex. KEDNE/PJM-10). For the test year, IRR's for total capital investments range from -7% to 125% and from -2% to 149% for marginal capital investments (Id.). Giving numbers in the aggregate does not prove that the free equipment program provides net benefits to ratepayers. Projects with larger IRR's could mask non-performing promotional programs. Thus, it could be that the free equipment program, the VPI program (discussed below) or another incentive program provides no net benefits to ratepayers, but because it is grouped together with high return projects for purposes of calculating the 18.8% IRR, the deficient program's failure is hidden. It could be that none of the promotional programs provide any net benefits to ratepayers and the alleged 18.8% IRR is due to capital investments that have nothing to do with promotionals. In either case, ratepayers would be paying for promotional incentives that, if separately analyzed, provide them with no net benefit.

In addition, the Company's selection of 25 year/15 year periods as the useful life terms for residential and commercial projects respectively is inordinately long. A quarter of a century was not the term utilized by the Department in evaluating the incentive program in the Berkshire Gas analysis. Moreover, an exact calculation cost benefit of residential conversion customers who received free equipment under the Company's promotional program was not provided. Since the burden of proof is upon the Company to demonstrate that there are net benefits to ratepayers from the free equipment program, and it has failed to do so. The Department should reject all costs associated with the free equipment incentive program.

3. All Costs and Expenses Associated With The Company's Value Plus Installer (VPI) Program Should Be Disallowed From The Cost of Service

To promote conversions of space and water heating customers to natural gas, the company instituted the Value Plus Installer (VPI) Program in 2000. This program enlists the assistance of appliance installation, service and repair contractors in the Company's efforts to entice consumers to undertake conversions. As part of this promotional program, the Company invites contractors to participate by promising specific benefits and advantages to those who become the VPI contractors. These benefits include receipt of qualified leads, subsidies for advertising costs, scheduling with potential conversion customers, access to training, incentive contests as set by the Company, and competitive contests with an all expenses paid trip as the top prize. (See Ex. MOC 2-4[a]).

Under the VPI Program, the service territories of the Company, and its sister companies Colonial and Essex Gas, have been divided into "lead distribution areas" ("LDAs") which are geographic territories for which a contractor can apply to become a VPI installer. The contractor must submit an annual fee of $1,000 for each LDA in which the contractor wishes to receives leads. This fee must accompany an executed contract entitled the Value Plus Installer Agreement Residential 1-5 Family which is a twelve month contract. (Id. p.19 et seq.). Once the contractor becomes a designated VPI contractor, the Company will obtain and provide customer leads, schedule appointments with customers, and assign leads to contractors through a rotation. (Id.)

Under the contract, a VPI contractor must satisfy certain obligations including: timely arrival for customers' lead appointments; performance of installations in a timely manner; maintaining liability insurance; maintaining and reporting current information on status of all customer leads assigned; providing customers with written price quotes for all work and materials; supplying of an executed contract if the installation includes free equipment; furnishing customers with a copy of a house heat survey for every gas equipment sale, if required; completion of all filings required by, and otherwise generally comply with, all federal, state, and local laws and regulations pertaining to the work performed by the installer; comply and agree to the company's evaluations concerning the quality of the contractor's work, performance and customer satisfaction with work performed; indemnification of the Company from any and all claims, liabilities, losses, and expenses in any way related to the installation work except due to the sole negligence of the Company; and an agreement to warranty the contractor's work. (Id. pp. 22-25).

In June of 2000, MOC and the Alliance filed a petition seeking a Department investigation of the implementation of the VPI Program by Boston Gas. Petition of Massachusetts Oilheat Council, Inc. D.T.E. 00-57 (2001). Among the various complaints was a challenge to the appropriateness of the program and whether ratepayer funds were being utilized to pay for the program. In its decision dismissing the petition, the Department indicated that since the costs of the VPI Program had not been approved to be part of the cost of service in the Company's prior rate case, the ratemaking treatment of the program should be deferred until the Company's next rate case (D.T.E. 00-57, p. 11). In this filing, the Company is seeking to recover the entire costs of the VPI Program, as well as the advertising costs associated therewith. (TR 3177, 3181-3182). MOC and the Alliance challenge the appropriateness of including these expenses in the cost of service.

As discussed above with respect to the Company's free equipment program, the intervenors believe that the standard to be applied to this program is two-fold. The threshold question is whether the program directly benefits the ratepayers. Boston Gas D.P.U.93-60 (1993). If the answer to the first question is in the affirmative, then the question is whether the evidence produced by the company demonstrates that the programs will provide net benefits to ratepayers. Berkshire Gas D.T.E. 01-56 (2002).

With regard to the initial question, the intervenors assert that if any benefits are derived from the VPI Program, they do not directly benefit the ratepayers. The Company contends that the entire VPI Program, including free trips for selected contractors to San Francisco, directly benefit ratepayers because the program encourages contractors to pursue customers to convert to natural gas "thereby increasing net revenues to the Company, thereby spreading the costs of all the fixed costs over a higher customer base and reducing rates for all customers". (TR 3432-3433). Even if correct, the Company's justification describes no direct benefit to ratepayers.

Ratepayers do not directly benefit from this contractor incentive program. Direct benefit implies that there is nothing in between the benefits offered through the VPI program and the benefit enjoyed by the ratepayer. It implies that the program should provide immediate advantages and value to the ratepayer who will experience first-hand personal benefits. Here, it is not possible for a ratepayer to even qualify for, or want, the direct benefits associated with the program. Residential customers can neither apply for nor take the direct advantages of cooperative advertising, training, and customer leads. Although many residential customers might want to win an all expense paid trip to San Francisco (Ex. MOC 1) those trips are limited to the VPI contractors who have performed a certain level of conversions. (Id.; see also Ex AG-3).

Another aspect of the VPI Program is that it consumes company management resources and expenses to duplicate what would normally happen in the marketplace. As seen from the VPI materials, the administration of the program is extensive (Ex. MOC 2-4[a]; 1-13[a][b]). Contract review, contractor qualifications verifications, handling, directing and assigning of market leads, customer contact, coordinating with contractors, reviewing and approving co-op advertising, customer follow-ups and evaluating contractor performance are among the many tasks performed by the Company under the VPI Program. (Id.)[3] The Company has not demonstrated that ratepayers are directly served by the administration and management of the VPI Program. There is no indication – and the Company has supplied no data – to suggest that the conversion work performed by contractors would not have been performed without the VPI Program.

The intervenors submit that the Company's monetary incentives, advertising subsidies, and free trips provided to contractors are inappropriate.[4] These contractors already profit from their installation and service work. Asking ratepayers to shoulder the Company's proposed rate increase while subsidizing contractors for conversion work that would be

[3] The Company contends it does not evaluate contractor performance or deal with customer complaints of contractors.(TR 2283-2284). This is inaccurate. In letters sent to customers following conversion, the Company asks for a contractor evaluation. (MOC Ex. 2; See also Ex. MOC 2-4[a] p.22).

[4] The Company disclosed that the trip to San Francisco cost $500,000 of which the New England portion was $75,000. (RR-DTE-111).

performed even without these incentives should not be countenanced.

Other than the alleged indirect benefit of adding load, which is in itself suspect, there is no economic or policy reason why contractors, including representatives from a company's own affiliate Key Span Home Energy Services, should be treated to an all expense paid vacation, rebate incentives, or given subsidization of their advertising costs, when such companies are profit-making entities. Apart from the havoc such an incentive program plays in the unregulated marketplace, there is no justification for placing the VPI Program on the backs of the ratepayers.

Even if the Department were to find that there is a direct benefit to the ratepayers from the VPI program, the Company must still prove that there is a net benefit to the ratepayer. The Company's economic justification for this trade ally program is the same 18.8% calculation for all its capital investments (TR 3437-3438). For the reasons previously set forth, MOC and the Alliance urge the Department to reject rate recovery for the VPI program for failure to meet the net benefits test (See Point VI.B.2.).

Finally, the intervenors request that the Department disallow all other promotional expenses from rate recovery for the same reason (See Ex. AG 23-1). Trade show expenses, rebates and other promotions should be excluded from the cost of service because they do not directly benefit ratepayers and provide net benefits.

4. The Company's Requested Advertising Amount Should Be Disallowed

Pursuant to M.G.L. c. 164, §33A, no gas or electric company may recover from its ratepayers any direct or indirect expenditures associated with promotional or political advertising. Exempted from this prohibition is advertising "which informs consumers of and stimulates the use of products or services which are subject to direct competition from products or services of entities not regulated by the department or any other government agency." (G.L. c 164, §33A). The Department has interpreted this statutory language to mean that cost recovery is permitted only when such expenses provide direct benefit to ratepayers. Boston Gas Company D.P.U. 93-60 p. 159 (1993); Bay State Gas Company D.P.U. 92-111 p. 201 (1992). See also Boston Gas D.P.U. 96-50 (1996).

In order to facilitate the review of advertisements for ratemaking treatment, the Department has delineated the manner in which a utility's advertisements should be classified. Advertising expenses must be categorized into four primary groups: (1) image-related; (2) informational; (3) promotional; and (4) miscellaneous. Boston Gas D.P.U. 93-60 at 162.

The promotional class must be further separated into:

(1) advertising which promotes the use of gas explicitly in competition with an unregulated fuel;

(2) advertising which promotes the use of gas but does explicitly reference an unregulated fuel; and

(3) advertising which promotes a company's non-utility operations.

Id. (footnote omitted). Establishment of these classifications was designed to enable the Department and intervenors to review expenditures in a more orderly and less time-consuming manner. (Id. p. 162, fn. 53).

In this proceeding, the Company seeks to recover $1.1 million in advertising expenses. (PJM/KEDNE Ex. 2, p. 24; Ex. AG-1). For the test year, the Company incurred $1,751,879 in advertising expenses (Ex. AG-1).[5] The Company removed from this expense image advertising of $75,986, informational/miscellaneous advertising totaling $37,661, and corporate image advertising $527,557 for a total adjustment of $641,204. (Id.).

While the Company believes that it has categorized its advertising consistent with the Department's precedent, a review of the advertisements themselves indicate that they are not so easily compartmentalized. Most, if not all, of the promotional advertisements utilized by the Company during the test year overlapped more than one of the categories. Some are clearly not entitled to rate recovery while others are questionable. A few examples will illustrate this confusion.

During the test year, the Company published and distributed a newsletter entitled "*Home News and Views*" Volume 4, Number 1 (Ex. AG-2). Although the Company identified the target audience for this newsletter to be "homeowners with pools that already have gas heating" (TR 108), the newsletter appears directed at general gas residential customers. A portion of the newsletter promotes the Company's free gas heating equipment program (Ex. AG-2 p. 4). However it contains non-promotional items such as a recipe for cooking baby back ribs (Id. p. 2), an invitation for customers to attend baseball games on Cape Cod (Id. p. 4), and an article on how to save electricity in warm weather which includes

[5] This figure may not include related administrative and labor expenses that are listed in the Company's 912 Account (Ex. AG 23-1).

suggestions to install awnings, close curtains, install appropriate landscaping, set air conditioning thermostats at higher temperatures. (Id. p. 4). None of these latter items fall within the statutory exemption for advertising expenses.

In addition, the ad promotes the use of gas pool heaters with a $200 rebate and the use of outdoor gas lighting with a $25 cash rebate for residential customers; other rebates for barbeque grills, heaters and fireplaces are offered as well (Id. pp. 1 and 3). Since promotion of gas lighting would be promoting the use of natural gas over electricity, an alternate energy source that is regulated, it does not fall within the statutory exemption of G.L. c 164, §33A. Similarly, promotion of gas pool heaters and fireplaces are, at least in part, directed at electric heaters and fireplaces. (See Ex. AG-39 and AG-40) and should also be disallowed. And, finally, the ad also announces the winner of a free natural gas grill. (Id. p. 2). The Department has stated that expenses associated with give-away items that promote good will are not recoverable in rates. (Boston Gas D.P.U. 93-60, p. 166).

Another newsletter produced by the Company entitled "*Trade Connection*" is sent to contractors who perform conversions from oil to gas. (TR 110). Volume 2, No. 1 of the *Trade Connection* newsletter issued during the test year contains a number of articles encouraging contractors to aggressively pursue conversions to natural gas. (Ex. AG-3). Also included in the newsletter is a leading article describing a Value Plus Installer's (VPI) trip incentive program ending April 30, 2002. According to the article, winners will be treated to round trip airline tickets for two, deluxe hotel accommodations, sightseeing and a "host of special VPI events in San Francisco" (Ex. AG-3 p.1).[6] Additionally, page 2 of the newsletter contains an article announcing the awards of cash giveaways for a competition among contractors for the most number of conversions performed during an 18 day period. (Id. p. 2). The newsletter also has a sidebar calendar of trade shows and training and an article entitled "another helpful sales tip" that contains an actual sales script for use by plumbers when approaching customers. (Id. p. 3). Advertising of the incentive trip, the trade show calendar, and sales tactics, are not promotional materials directed at customers to encourage their use of natural gas over competing non-regulated fuels and provide no direct benefits to ratepayers. Consequently, the cost associated with these advertisements should not be permitted to be recovered through rates.

Significantly, all advertising expenses associated with and directed at contractors should be disallowed since such costs are not authorized by statute. Pursuant to G.L. c 164, §33A, the exemption to the prohibition of utility promotional advertising only includes advertising which: "informs consumers of and stimulates the use of products or services which are subject to direct competition from products or services of entities not regulated by the Department or any other government agency." (emphasis added). The statute only carves out an exemption for advertising to consumers. Advertising directed at HVAC, building or any other contractors are not mentioned. Under a plain reading of the statute, all direct and indirect advertising costs aimed at contractors should be disallowed.

In addition to HVAC contractors, the Company has included in its advertising

[6] The cost of the incentive trip itself was discussed above.

cost materials produced to encourage builders to promote the use of natural gas in homes. One particular piece fosters the installation of natural gas to housing developments. It offers "marketing support materials" which includes directional signs to building projects (See Ex. AG-4). The signs display the KeySpan Energy Delivery logo. These materials do not meet the statutory requirements of recoverable promotional materials since they are not directed at the ultimate consumer and since they do not directly benefit the ratepayer.

Another promotional advertisement entitled "other uses for natural gas energy" was directed at commercial and industrial customers during the test year (Ex. AG-6, TR 136). Although a paragraph discusses the installation of gas hot water heaters, the remainder of the ad promotes natural gas in competition with electricity or promotes natural gas vehicles. The ad encourages customers to satisfy their electric needs with distributed generation and promotes natural gas cooling and refrigeration over electric units. The Department has, in the past, rejected advertisements relating to NGV promotions. (Boston Gas D.P.U. 96-50, p. 64.) Similarly, since electric products and services are regulated by the Department, the costs associated with this advertisement should be disallowed.

A review of the ads supplied by the Company (see Ex. AG 1-73[b]), confirms the Company’s practice of combining advertisements. This collection contains a number of ads promoting conversions for fireplaces, pool heaters, spa heaters, patio lights, and BBQ grills. Another "*Home News and Views*" newsletter (Volume 4 No. 2) advertises “All American BBQ” recipes, water conservation tips, pool safety, a calendar of events, and seminars held by Home Depot unrelated to heating appliances (i.e., hanging wall paper, lawn care, etc.) (Ex. AG 1-73[b]).

The presented examples demonstrate a pattern of mixed advertising. Non-recoverable and possibly recoverable advertisements are combined. Rebates and giveaways are offered. The Company has not categorized its advertising in a manner which allows the Department and intervenors to review these expenditures in an orderly and efficient manner. (Boston Gas D.P.U. 96-50; Boston Gas D.P.U. 93-60). The intervenors recommend that the Department limit its approval of the Company's expenses to those advertisements that fall squarely within the statutory exemption.

C. THE DEPARTMENT SHOULD ORDER THE COMPANY TO PROVIDE POTENTIAL CONVERSION CUSTOMERS WITH A FULL COST DISCLOSURE STATEMENT, A PAYBACK ANALYSIS AND A DISCLAIMER IN ITS GUARANTEE

KeySpan's implementation of its conversion programs including the free equipment giveaways, rebates and advertisements will continue to capture consumer attention. To assure that consumers are provided with accurate information prior to undertaking a conversion, the Department should order the company to provide potential conversion customers with a cost disclosure statement detailing all the expenses associated with conversion together with an analysis estimating the payback period for the costs associated with undertaking such a conversion. Both the statement and analysis would provide consumers with factual accurate and unbiased information to assist customers in making an informed choice as to whether conversion from one energy source to natural gas is within the consumer's particular financial interest.

Assuming, *arguendo*, that such conversions are economical and beneficial for the utility, this may not be so for the conversion customer. Conversion from an alternate heating system to natural gas involves significant capital investment for the average homeowner. The period of time necessary for the customer to recoup this investment is an essential piece of information. This is especially important this coming winter when higher natural gas prices are anticipated.

The Company has indicated that regardless of price, it intends to pursue its free equipment program and to aggressively promote conversions. Therefore, before customers are enticed to undertaking such conversions, they should be fully informed of the full costs of such conversion through a disclosure statement, and should possess personalized financial payback information to enable the customer to make this significant financial choice fully informed with factual information.

The Company does not presently offer any payback analysis to the customer because, it contends, that it does not know the costs of the equipment being installed (Ex. MOC 2-2) nor the labor costs (TR 2289).[7] This is no excuse. Plainly, a payback analysis form can be produced where the customer's individual equipment and labor costs can be added and then arithmetically computed utilizing, among other information, the existing price of gas, the AFUE rating of the equipment, and contemplated usage to determine an estimated payback period.

The necessity for a full disclosure statement and a payback analysis is made all

[7] At present, when potential conversion customers ask about the price of natural gas, they are given the rates for natural gas. (Ex. MOC 2-3). If customers ask about the price of natural gas versus oil they are provided with two charts. (Id.) Neither are current and neither constitutes a customized personal evaluation for the customer.

the more imperative by the Company's promotional programs. In light of advertisements that offers free heating equipment, rebates for removal of oil equipment, and free hookup line up to 100 feet, consumers will believe that such a conversion will be of little or no cost to them.[8] Customers may believe that by being offered free equipment and rebates, the conversion will cost little and the payback period for the conversion costs will be brief. An arithmetic computation will give the consumer a reality check on the Company's enticements.

Another reason that a payback analysis is necessary stems from the Company's satisfaction guarantee. As part of its conversion program, KeySpan offers a "guarantee of satisfaction" that states, in part:

> "If for any reason you are not satisfied with natural gas heat after two years from the date your equipment was installed, KeySpan Energy Delivery will arrange to remove the equipment and will refund your equipment and installation costs to you".

(Ex. MOC 5-12, p. 2).

The Company's honoring of its guarantee would not make a dissatisfied customer whole. Under the guarantee a customer would only have the gas equipment removed and the equipment installation costs refunded. It does not cover the reinstallation of a heating system (TR 2264). The customer would have no heating system and would have to incur the additional equipment and labor costs to install an alternate heating system. This actually operates as a disincentive to dissatisfied customers.[9]

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[8] A statement reminding the customer that the possibility of high gas prices should be considered in making a conversion decision could also be included.(See Point VI.B.1.)

[9] The Company states that no one has taken advantage of the guarantee. (Ex. MOC 5-12, TR 2264).

Full disclosure is warranted. The enticement of free heating equipment and other promotions as well as a guarantee of satisfaction may leave conversion customers to believe that the offer is risk free. In addition, the intervenors urge the Department to require the Company to include an affirmative statement in its guarantee of satisfaction that the cost of the equipment and installation of an alternate energy system is not covered by the guarantee.

It is equitable and fair for consumers to know the entire costs involved in a conversion as well as a payback term prior to making a conversion decision. Full cost disclosure, full disclosure of the extent of the Company's guarantee, and a payback analysis is in the public interest, provides consumers with facts and accurate economic information related to their own specific and particular heating circumstances, and enables them to make an informed intelligent choice as to whether conversion makes economic sense to the particular customer.

D. THE DEPARTMENT SHOULD REQUIRE THAT THE COMPANY'S UNREGULATED HVAC AFFILIATES HAVE NAMES THAT ARE DIFFERENT FROM THE COMPANY

Since its last full rate case, Boston Gas has been acquired by the KeySpan corporate conglomerate and is now part of the KeySpan collection of companies. The collective corporate structure is such that some operations that once were with the regulated utility now reside with a service company or elsewhere for administrative purposes. The Company proclaims the "synergies" of such an arrangement as being beneficial to all its corporations, including the Company because of cost savings. In reality, it is difficult to fully understand the Company's workings and its full inter-relationship with the other KeySpan family companies.

Primarily contributing to this confusion is the fact that virtually every KeySpan company involved in energy and HVAC services bears the word "KeySpan" somewhere in its name. It is easy to confuse and misunderstand operations, policies, and applications associated with each entity. This is especially significant since the Company is a regulated entity and many of the affiliate companies are unregulated. While the Company has attempted to draw a clear line between all its corporations, the reality is that the line is blurred.

Under the Department's regulations governing affiliate conduct, an affiliate's use of the LDC's name or logo is currently permitted. The provisions of 220 C.M.R. 12.00 et seq. entitled "Standards of Conduct for Distribution Companies and Their Affiliates" defines the nature of the relationship and transaction of gas and electric companies and their affiliates. Subdivision 11 of §12.03 states:

> A distribution company shall refrain from giving any appearance of speaking on behalf of its competitive affiliate in any and all contacts or communications with customers or potential customers. The distribution company shall not represent that any advantage accrues to customers or others in the use of the distribution company services as a result of that customer or others dealing with a competitive affiliate.

Applying the above language, the distribution company would be the Company and the competitive affiliate would be KeySpan Home Energy Services, Inc.[10]

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[10] Competitive affiliate is defined as any affiliate that is engaged in the sale or marketing of products or services on a competitive basis (220 C.M.R. 12.02[3]). This is

Similarly, Sections 12 and 13 of 220 C.M.R. 12.03 state, in pertinent part, as follows:

> (12) The distribution company shall not engage in joint advertising or marketing programs of any sort with its competitive energy affiliate, nor shall the distribution company directly promote or market any product or service offered by any competitive affiliate.
>
> (13) Subject to paragraph (12), a Distribution Company may allow an Affiliate, including a Competitive Energy Affiliate, to identify itself through the use of a name, logo, or both, as an Affiliate of the Distribution Company, provided that such use by a "Competitive Energy Affiliate" shall be accompanied by a disclaimer that shall state that no advantage accrues to customers or others and the use of the Distribution Company's services as a result of that customer or others dealing with the competitive energy affiliate, and that the customer or others need not purchase any product or service from any Competitive Energy Affiliate in order to obtain services from the Distribution Company on a non-discriminatory basis. The disclaimer shall be written or spoken, or both, as may be appropriate given the context of the use of the name or logo.

Every one of KeySpan's ads gives the appearance that the Company is speaking on behalf of its competitive affiliates, particularly with regard to conversions. Use of the ubiquitous KeySpan logo, as part of the Company's overall branding strategy, as part of its promotional advertisements, and elsewhere, is identical to the KeySpan logo that is utilized by all the affiliates of the KeySpan galaxy of companies. It does not take much to realize that when the Company issues promotional advertising with the name and logo KeySpan affixed, it gives the appearance to the public that the Company is speaking on behalf of its competitive

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opposed to a competitive energy affiliate that refers to an affiliate engaged in the sale of marketing of natural gas and electricity and related services (220 C.M.R. 12.02[4]).

affiliate, KeySpan Home Energy Services.

The omnipresence of the KeySpan logo is exactly what is intended by the Company's "branding" strategy which, as described by the Company witness, is anything used to get the KeySpan name out to consumers in New England (TR 103-104).[11] The Company pays a fee for this branding service to KeySpan's service corporation and has removed "branding" expenses from the cost of service (Ex. AG 1-78). However, the ability to separate "branding" costs versus promotional expenses on an accounting ledger is not so easily accomplished in the marketplace. In reality, the unregulated affiliates not only have the advantage of the promotional advertising conducted by the Company, they also benefit from the branding program. In terms of embedding the KeySpan name in the public conscience, the two are indistinguishable and the Company admits that all advertising is a form of branding (TR 105).

From a competitor's standpoint, members of the Alliance and MOC have to compete with HES and the Company in a marketplace where all of the branding and image advertising, as well as any rate recoverable promotional advertising appear, for all practical purposes, as if they originate from the same entity. From a consumer there is little distinction. Aside from maintaining some semblance of separation, the Company's own actions fail to clearly delineate the relationship between the Company and HES in the marketplace. Several

[11] The KeySpan collection of companies totals about 107 entities (Ex. AG 17-9). Of these over 60 companies have the name "KeySpan" in either the corporate name and/or in its d/b/a. (Id. Attachment).

examples will highlight this fact.[12]

KeySpan Corporate Services, LLC is responsible for designing, maintaining, upgrading and monitoring the overall KeySpan website located at www.keyspanenergy.com (Ex. MOC 3-3). The Company was allocated $207,800 from the service company for web management expenses (Id.). When accessing the KeySpan website relating to the Boston, Massachusetts region, a site map can be reached at www.bostongas.com/sitemap/index/_ma_kedma.jsp (Ex. MOC 3-4). At that page, there is a list of categories that can be clicked to view another page on the site. Under the heading "*Products and Services for Home*", there is a link *"Installations, Repair and Service Plans*". Clicking on this link will take the user to the Home Energy Service web page located at www.keyspanenergy.com/ps/home/equipped/index_ma_kedma.jsp (Id.). Similarly, at the Boston Gas site map under the heading "P*roducts and Services for Business*", clicking the link "*Heating and Cooling Services*" takes the user to Home Energy Services web page located at www.keyspanenergy.com/psbusiness.heat_cool/index_ma_kedma.jsp. (Id.).

Significantly, Home Energy Services has no separate website. (Id.) Instead, its entire web presence is located on the KeySpan corporate website. While other links on the web page can connect the user to the utility's VPI program (of which a HES is a participant), links generally connect to the Company's unregulated affiliate. The intervenors are unaware of any unregulated Company that has the same type of benefit as HES. Competitors in the HVAC

[12] Although the examples may point to alleged violations of the standards of conduct, the intervenors are not pursing remedies for those violations here other than to urge the Department to order the Company's unregulated HVAC affiliate to adopt a corporate name that does not have the name "KeySpan" in its title.

market must either purchase, maintain and operate their own websites or do not have a web presence at all. Again, the manner and method by which the website is constructed gives the impression to the public that the Company, as well as all the other companies, are speaking on behalf of the competitive affiliate HES (220 C.M.R. 12.03[11]) and constitutes a direct promotion or market of products or services offered by HES (220 C.M.R. 12.02[12]):

On January 29, 2002, HES ran an ad in the *Boston Herald* entitled "Its Time for a New Flame" (Ex. AG-7). KeySpan Home Energy Services is a participant in the Company's VPI program. This ad promotes the free equipment program of the Company, as well as claiming, "switch to gas heating now - - a promising new relationship awaits" (Id.). In extremely fine print at the bottom of the ad, there is some critical customer information regarding monetary contribution if the boiler is over 105,00 BTUs, that removal of the oil tank will cost extra, the duration of the KeySpan Energy Delivery offer, and that KeySpan Energy Delivery offer may not be combined with any KeySpan Home Energy Services offer. There is also a statement that purchase from HES has no effect on the availability, price or terms from KeySpan Energy Delivery (Id.).

The "New Flame" ad demonstrates the confusion generated by the joint advertising by two "KeySpan" companies. While the unregulated subsidiary and the Company may have conceived and split the financing of this advertisement, (See RR-AG- 9) the two companies are virtually indistinguishable in the ad. The word "KeySpan" in both Company names does nothing to distinguish the two companies. Significantly, the fact that HES does not permit its own incentives to be combined with the Company's free equipment offer also further confuses the reader as to the relationship between the two companies. The existence of the disclaimer, while welcome, is too small and uninformative to create a distinction between the Company and its unregulated affiliate.

As if the similarity of names was not a significant problem, HES receives advertising funding. Despite all the publicity and exposure that KeySpan Home Energy Service receives from the Company and the KeySpan conglomerate, HES also received in the test year the amount of $17,000 in advertising subsidies from the Company (RR-MOC-5). As a participant in the Company's promotional VPI program, HES was entitled to apply for and receive cooperative advertising reimbursements. These advertising costs paid by the Company are sought to be recovered in rates. The ratepayer is being asked to pay for advertising that, given the similarity of name, is simply unnecessary.

To eliminate confusion with consumers, to insure that KeySpan Home Energy Services and other non-regulated KeySpan companies do not have the tremendous advantage in the competitive marketplace of being associated with the monopoly utility company, the Department should order that all affiliates of the Company engaged in appliance service, repair and installation be operated and conducted under a name that is distinctly different from the KeySpan name and does not have the KeySpan name or logo in its trade name or servicemark. Furthermore, to the extent that any of its competitive affiliates such as KeySpan HES change their name, they should be prohibited from utilizing the KeySpan brand logo in its advertisements, on its trucks, or elsewhere. Consequently, we respectfully request that the Department amend its standards of conduct with respect to the Company in this regard.

E. THE DEPARTMENT SHOULD REQUIRE THE COMPANY'S NEW AND EXISTING INTERRUPTIBLE CUSTOMERS OF THE COMPANY TO HAVE SUFFICIENT BACK-UP SUPPLIES OF ALTERNATIVE FUEL AVAILABLE FOR PERIODS OF INTERRUPTION

Intervenor MOC is comprised of members who are small and medium sized businesses who sell service and deliver heating oil and oil heat equipment to residential, commercial, and industrial customers. MOC members are the final link in the Commonwealth's vital petroleum distribution chain and are suppliers of the heating oil used by interruptible natural gas consumers. Interruptible gas customers often include large volume industrial, commercial, or institutional entities such as manufacturers, apartment complexes, government buildings, hospitals, schools, and electric generators. These consumers are permitted to purchase inexpensive, excess supplies of natural gas with the provisio that the Company can interrupt their supply of natural gas at any time. When an interruption occurs, adequate supplies of alternate fuel must be available to assure continuous operation.

The alternate fuel most often used by interruptible customers is petroleum. Since interruptions ordinarily occur during winter periods of peak energy demand, the sudden entrants of these large volume gas interruptible customers into the petroleum market can and has placed a strain upon the petroleum supply and delivery infrastructure. In turn, this strain not only disrupts the supply/demand balance in the marketing base, but also often causes the price of heating oil to spike, directly increasing costs to residential and commercial heating oil customers. From December 9, 2002 to March 31, 2003, the Company reported 113 days of interruption due to extended cold weather forecasts (Ex. MOC 5-1). Consequently, MOC has a direct and significant interest in establishing predictable demand to the fullest extent possible by the orderly, non-disruptive entrance of interruptible gas users into the heating oil market during periods of peak demand.

Despite the tremendous competition that exists between oil distributors and natural gas utilities, the inter-dependence of the gas and petroleum industries, as well as the electric industry, has become more apparent in recent years. This is particularly true with regard to interruptible customers, some of whom are electric generators. The reliability of each energy infrastructure, as well as the supply and price of each product, depends at least in part on the proper management of the unexpected demand created by interruptible customers during peak winter periods.

The Company has indicated that it has not required interruptible customers to maintain dual fuel capability consistent with the Department precedent. In Interruptible Transportation, D.P.U. 93-141-A (1996), the Department stated:

> The Department finds that a dual-fuel capability requirement is not necessary to insure the efficient operation of the distribution system or the safe and efficient delivery of gas to interruptible customers. Therefore, the department directs LDCs to develop terms and conditions which do not incorporate a requirement for dual-fuel capability. However, the department expects that LDCs will propose a set of criteria to be met by IT customers, to demonstrate that they are capable of either ceasing operations or switching to an alternate fuel if IT is not available on the LDCs' distribution system. Additionally, LDCs should develop reasonable charges or other penalties that would deter the unauthorized use of the distribution system by interruptible customers.

D.P.U. 93-141-A (1996) at p. 47.

In accordance with this order, the Company's Interruptible Transportation Agreement contains a certification by the customer that it "has and maintains the ability to utilize an alternative fuel or that it has taken such other measures as it deems appropriate to assume the risk that service hereunder may be uninterrupted…" (Ex. MOC 5-4, Attachment p. 2, Section 3.1). MOC respectfully submits that it is time for the Department to modify its position and require that interruptible customers have back-up fuel on hand and available for periods of interruption.

In December of 2000 the United States Department of Energy issued a report prepared jointly by the Office of Policy and the Energy Information Administration entitled "The Role of Interruptible Natural Gas Customers in New England Heating Oil Markets: A Preliminary Examination of Events in January - February, 2000", dated November 2000. (See Attachment to Ex MOC 5-7). The report responded to information gathered following a price spike in oil resulting from a severe cold weather snap in January and February 2000. Significantly, the report found that the purchasers of distillate fuel oil by interruptible natural gas customers may have contributed to the spike in the price of distillate during the peak weeks of gas interruptions. While the entrance of interruptible gas customers onto the heating oil system was not the sole and/or most significant cause of price increases, it was a contributing factor. Therefore, the report concluded:

> . . .several steps should be taken to reduce the potential adverse impacts of gas supply interruptions in times of market stress without undermining the benefits of interruptible service.

(Id. p. 12).

Among the recommendations was the possible solution of increasing storage levels of back-up fuels by interruptible gas customers:

> To the extent that consumption of distillate fuel oil by

> interruptible gas customers during periods of severe winter weather could be derived from inventories rather than near-term purchases, the impact of their demand on distillate fuel oil prices would tend to be lessened. States could require the interruptible gas customers using distillate fuel oil as a back-up fuel have at least some minimum volume of inventory on-site (and/or under contract if a customer's on-site storage capacity is limited).

(Ex. MOC 5-7 Attachment p. 13).

The Department of Energy's report focused mainly on the interruptible impact upon the distillate market, with which MOC is greatly concerned. However, advanced planning and proper management inures to the benefit of the natural gas market as well. Lack of planning on the part of large-volume interruptible natural gas customers and the absence of an orderly transition of these customers from the gas market to the heating oil market, can severely impact both industries. The impact upon the petroleum markets has been recognized. Similarly, the inability of interruptible customers to transfer to the heating oil market and who remain on gas could place additional strain upon the natural gas market thereby constraining supplies and possibly raising prices. To the extent that electric generators rely on distillate product for their back-up fuel, the ability to generate electricity is placed in jeopardy if neither the heating oil market nor the natural gas market can supply energy for generation.

As the Commonwealth's petroleum storage infrastructure declines, the potential that a severe winter will have a severe impact upon all energy consumers becomes greater with each passing year. It is sensible for interruptible customers to have adequate storage capacity and inventory on hand during extended cold periods not only as a buffer to demand, but also to moderate price increases during such high demand periods. Maintaining sufficient storage capacity and inventory for use during periods of interruption would be consistent with the Federal Government's recommendation and with other states' approaches.[13]

Intervenor MOC therefore requests that the Department establish a requirement that the Company's interruptible customers have minimum back-up fuel for a period determined sufficient by the Department. Prior to the commencement of a heating season, the Company should inform each of its interruptible customers to secure adequate alternate fuel supplies for the upcoming heating season. New customers applying for interruptible service from the Company should be required to have actual on-site storage and inventories prior to the commencement of the heating season in an amount to be determined by the Department.

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[13] See for example New York PSC Case 00-G-0996 establishing a 7/10 day back-up fuel requirement for temperature control and demand interruptible customers respectively. (Orders dated August 24, 2000 and January 31, 2001).

VII. CONCLUSION

MOC and the Alliance respectfully request that the recommendations set forth above be adopted by the Department.

Respectfully submitted,

Massachusetts Oilheat Council, Inc.
and Massachusetts Alliance for Fair
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